GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF TAX AND REVENUE

NOTICE OF PROPOSED RULEMAKING

The Office of Tax and Revenue (OTR), pursuant to the authority set forth in the D.C. Official Code § 1-204.24c, as amended by Section 155 of the District of Columbia Appropriations Act 2001, approved November 22, 2000 (114 Stat 2476; Pub. L. 106-522) and the Office of the Chief Financial Officer, Financial Management and Control Order No. 00-5, effective June 7, 2000, hereby gives notice of his intent to adopt new Taxation Regulations. The proposed regulations will add a new Section 109 to Chapter 1 of Title 9 of the D.C. Municipal Regulations (DCMR).

The proposed regulations will delete present Section 109 of Chapter 1 of Title 9, District of Columbia Municipal Regulations Sections 109 through 109.5, substituting therefor Sections 109.1 through 109.99.

The following new Section 109, **CONSOLIDATED RETURNS TAX REGULATIONS**, is added to Chapter 1 of Title 9 DCMR:

109 CONSOLIDATED TAX RETURNS

109.1 District of Columbia affiliated group means an "affiliated group" as defined in §1504 of the Internal Revenue Code of 1986, as amended (IRC). Generally, District of Columbia affiliated groups shall not include any corporation that does not have gross income derived from sources within the District and nexus to the District of Columbia. Members of an affiliated group that are exempt from District taxation cannot be included in the consolidated return.

(a) District of Columbia affiliated group may not include any corporation, which is a Qualified High Technology Company as defined in D.C. Official Code § 47-1817.01(5)(A) (a QHTC) and those corporations, described in IRC § 1504(b). A QHTC may opt out of status under D.C. Official Code §47-1817.01(5)(A) and be eligible to be included in a District of Columbia affiliated group. See §109.40.

(b) If a Qualified High Technology Company that has not made an election under §109.40 ceases to be a Qualified High Technology Company, such corporation (and any successor of such corporation) may not be certified as a Qualified High Technology Company before the 61st month beginning after its first taxable year in which it ceased to be a Qualified High Technology Company. During this period, such corporation is not eligible to make an election under §109.40.

(c) Each member of a District of Columbia affiliated group shall be jointly and severally liable for the taxes, interest and penalties of the District of Columbia affiliated group. If a corporation is a member of the District of Columbia affiliated group for a part of the year, then the corporation shall be liable for the tax liability attributed to that portion of the year that the corporation was a member of the District of Columbia affiliated group.

(d) The "gross income derived from sources within the District" requirement in D.C. Official Code §47-1805.02(5)(D) is waived for a corporation that meets the following requirements:

(1) A member of a regulated industry whose revenue is determined by means of a rate-setting procedure by a federal government agency, but only where the regulatory requirements to which the industry is subject impose restrictions on the structure of the affiliated group,

(2) A member of an affiliated group as defined in §1502 of the IRC, and

(3) In a trade or business in the District.

109.2 All members of a District of Columbia affiliated group must use the same accounting method and the same accounting period.

(a) Unless otherwise provided by these rules or inconsistent with the provisions of the D.C. Official Code, the consolidated taxable income for a District of Columbia consolidated return year shall be determined in the same manner and under the same procedures, including intercompany adjustments and eliminations, as are required by the federal consolidated return regulations.

(b) All intercompany transactions between and among members of a District of Columbia affiliated group will be eliminated in determining the District of Columbia apportionment factors.

(c) An intercompany transaction is a transaction between corporations that are members of the same District of Columbia affiliated group immediately before and after the transaction.

(d) Any deferred gain, loss or deduction from a prior transaction with a member of a District of Columbia affiliated group shall be recognized for District of Columbia purposes when the member subsequently ceases to be a member of that District of Columbia affiliated group or when the asset involved is transferred to a corporation which is not a member of District of Columbia affiliated group.

(e) All supplementary and supporting schedules filed with a District of Columbia consolidated return shall be prepared in columnar form. One column being provided for each corporation included in the consolidated return, with the parent corporation information reported in the first column. Supporting schedules for the consolidated return shall also include a column for totals of like items before adjustments are made, a column for intercompany eliminations and adjustments, and a column for totals of like items after giving effect to the eliminations and adjustments.

109.3 Each member of a District of Columbia affiliated group must have gross income in any amount derived from sources within the District of Columbia.

(a) In the case of a corporation that is a member of the District of Columbia affiliated group for a part of the taxable year, the District of Columbia consolidated return shall include the income of the corporation for only that part of the year that it is a member of the District of Columbia affiliated group. If the new member is an existing D.C. corporation and not a member of another District of Columbia affiliated group, a final

short-year separate year return must be filed for the period prior to becoming a member of the affiliated group. If the new member was a member of another District of Columbia affiliated group, its taxable income or loss for the period prior to joining the new District of Columbia affiliated group must be included in the consolidated taxable income of its prior District of Columbia affiliated group. Correspondingly, if a member leaves a District of Columbia affiliated group, its taxable income or loss for the remainder of the taxable year shall be reported on a separate short-year tax return or included in the consolidated tax return of its new District of Columbia affiliated group, where permissible under these rules.

(b) District Taxable Income is computed as if a consolidated federal corporate income tax return was filed that included all Affiliates.

(c) The following are computed on a consolidated basis as if all Affiliates were a single corporation filing a District corporate income tax return:

(1) District adjustments and allocation of business income;

(2) Apportionment: Intergroup Transactions are eliminated when computing apportionment factors (See 9 DCMR §§ 109.20);

(3) Net Operating Loss;

(4) District Taxable Income is computed on a consolidated basis;

(5) District Franchise Tax;

(6) District Tax Credits; and

(7) Election and Revocation in accordance with 9 DCMR §§ 109.4 and 109.6.

109.4 In order to file a District of Columbia consolidated return; the members of a District of Columbia affiliated group must be part of the affiliated group that files a federal consolidated return pursuant to §1501 of the IRC.

(a) If a group wishes to exercise its privilege of filing a consolidated return, such consolidated return must be filed not later than the last day prescribed by law (including extensions of time) for the filing of the common parent's return. Such consolidated return may not be withdrawn after such last day.

(b) The election made by the common parent is effective prospectively and only if accompanied by a written consent to the election signed by each member of the District of Columbia affiliated group. The completed written consent of all members shall be attached to the District of Columbia consolidated return for the taxable year for which the election is made.

(c) Election to file a consolidated return is binding to the District of Columbia affiliated group for the first year of election and for subsequent years as long as the District of Columbia affiliated group remains in existence, unless a written request for revocation is submitted to the Office of Tax and Revenue and the Office of Tax and Revenue grants permission to a group to discontinue filing consolidated returns.

(d) The making of a District consolidated return shall be upon the condition that all corporations which at any time during the taxable year have been members of the affiliated group consent to all the consolidated return regulations prescribed under Title 9 of the District of Columbia Municipal Regulations prior to the last day prescribed by law for the filing of such return. The making of a District consolidated return shall be considered as such consent.

(e) If an eligible corporation becomes a member of the District of Columbia affiliated group after the beginning of the District of Columbia consolidated return year or ceases to be a member of the District of Columbia affiliated group during the consolidated return year, two tax returns will be due for that taxable year. The District of Columbia consolidated return shall include amounts attributable to such corporation for the part of the year in which it was a member of the District of Columbia affiliated group. A separate return shall be filed and include the amounts attributable to such corporation for the short taxable year when it was not a member of the District of Columbia affiliated group.

109.5 In taxable years after the election, any corporation deriving gross income, in any amount, from District of Columbia sources that was not a member of the original federal affiliated group in the year of the election but is a member of the federal affiliated group in the current year shall be required to join the District of Columbia affiliated group.

(a) The new corporation shall be deemed to have waived any objection to the filing of the District of Columbia consolidated return by its consent, if any, to join in filing a District of Columbia consolidated return by the common parent of the District of Columbia affiliated group.

(b) The new member joining the District of Columbia affiliated group shall be required to consent to the election to file a District of Columbia Consolidated Corporation Franchise Tax Return. A written consent shall be attached to the District of Columbia consolidated return for the first taxable year in which the new member joins the District of Columbia affiliated group.

109.6 The election shall terminate automatically upon the revocation or termination of the federal consolidated election, and the common parent shall notify the Office of Tax and Revenue within thirty (30) days regarding the revocation or termination of the federal consolidated election.

(a) If the District of Columbia affiliated group wants to revoke the election in a subsequent tax year, the group must request in writing and receive written permission from the Office of Tax and Revenue. The request to discontinue filing a D.C. consolidated return must be made at least ninety (90) days before the due date (including any extension of time for filing) of the return.

(b) If the request for revocation or termination of District of Columbia consolidated election is denied by the Office of Tax and Revenue, the District of Columbia affiliated group may file a written protest and request a hearing within thirty (30) days from the denial date.

(c) If a corporation has ceased to be a member of District of Columbia affiliated group and if such cessation resulted from a bona fide sale or exchange of its stock for fair value and occurred prior to the date upon which any deficiency is assessed, the

Office of Tax and Revenue may make an assessment and collect the deficiency from the former member.

109.7 If the District of Columbia affiliated group files a consolidated return for the first year of filing, it must make payment of estimated tax on a consolidated basis for subsequent years. The District of Columbia affiliated group is treated as a single corporation for purposes of D.C. Official Code 47-1812.14(a) (relating to payment of estimated tax by corporations) and D.C. Official Code 47-1812.14(b) (relating to underpayment of estimated tax by corporations).

(a) If separate returns are filed by the members of the District of Columbia affiliated group for the taxable year after receiving consent for discontinuance from Office of Tax and Revenue, the amount of any estimated tax payments with respect to a consolidated payment of estimated tax for such year will be credited against the separate tax liabilities of the members in any manner designated by the common parent which is reasonably satisfactory to the Office of Tax and Revenue. For example, the manner of allocation will be satisfactory to the Office of Tax and Revenue if it does not jeopardize the collection of the corporation franchise tax liability from such members.

(b) Supporting schedules shall be filed with the District of Columbia consolidated tax return for each member. The statement of gross income and deductions and other schedules required for each corporation shall be prepared and filed in columnar form so that the details of the items of gross income, deductions, and credits for each member may be readily ascertained. A column shall also be provided giving effect to any eliminations and adjustments. The items included in the column for eliminations and adjustments should be symbolized to identify contra items affected, and suitable explanations appended, if necessary. Similar schedules shall contain a columnar form of reconciliation of retained earnings for each corporation, together with a reconciliation of consolidated retained earnings. Consolidated balance sheets at the beginning and close of the taxable year of the group shall accompany the consolidated return prepared in a form similar to that required for other schedules. Transactions with a subsidiary which is not included as part of the District consolidated return shall not be considered as intercompany transactions for elimination purposes in computing the consolidated District taxable income for the return period.

109.8 Federal Taxable Income is computed as if a consolidated federal corporate income tax return was filed that included all Affiliates. Federal Treasury regulations under 26 Code of Federal Regulations §1.1502 *et seq*. and interpretations thereof regarding intercompany transactions apply in determining the federal taxable income of a District consolidated group.

109.9 ALLOCABLE INCOME [Reserved]

109.10 The following adjustments may be made under these regulations:

(a) Nothing herein shall prevent the exercise of authority under D.C. Official Code § 47-1810.03 to distribute, apportion, or allocate income or deductions between or among corporations where such action is necessary in order to prevent evasion of taxes or clearly to reflect the income of any such corporation. OTR also has the

authority to determine whether such method should be followed on a consistent basis, from year to year.

(b) The District may require that a consolidated return be filed under D.C. Official Code § 47-1805.02(D)(5)(C)(iv) for an affiliated group that is eligible but where an election to file a consolidated return has not been filed if the District determines that a consolidated return is necessary to prevent evasion of taxes or to clearly reflect the taxable income that is attributable to the business conducted in the District by the affiliated group.

109.11-
109.19 [Reserved.]

109.20 The three-factor apportionment requirements of D.C. Official Code §47-1810.02(d) shall be taken into account by an affiliated group doing business within and without the District of Columbia. All members of an affiliated group which join in the filing of a District consolidated tax return shall be considered as one "person" to determine the portion of the consolidated net income earned within and without the District by the same method prescribed in the statute cited above. All intercompany transactions shall be eliminated in the determination of the apportionment factors.

(a) A single consolidated apportionment factor is constructed for the affiliated group. The property, payroll, and sales factors include the property, payroll, and sales for all members of the consolidated group. The consolidated apportionment factor constructed is then multiplied by the consolidated adjusted federal income to determine the adjusted federal income apportioned to the District of Columbia.

(b) The members of the affiliated group may not determine separate apportionment factors to apply to their portion of the consolidated adjusted federal income.

(c) The District property factor for the consolidated group shall be determined pursuant to D.C. Official Code §47-1810.02(e) and 9 DCMR §§ 125 and 126.

(d) The District payroll factor for the consolidated group shall be determined pursuant to D.C. Official Code §47-1810.02(f) and 9 DCMR §§125 and 127.

(e) The District sales factor for the consolidated group shall be determined pursuant to D.C. Official Code §47-1810.02(g) and 9 DCMR §§ 125 and 128.

(f) Where all members of the consolidated group are subject to a special apportionment formula provided by D.C. Official Code §47-1810.02(h), and approved by the Office of Tax and Revenue, the consolidated group will determine a single consolidated apportionment factor using the special formula. Where all members of the affiliated group are not subject to the identical special formula approved by the Office of Tax and Revenue, the special formula is not available to the affiliated group.

(g) Under D.C. Official Code §47-1810.02(h), the following alternative methods may be requested or prescribed in respect to all or a part of taxpayer's business activity where necessary to fairly represent the extent of taxpayer's business activity in the District:

(1) Separate accounting;

(2) The exclusion of any one or more of the factors;

(3) The inclusion of one or more additional factors that will fairly represent the taxpayer's business activity in the District; or

(4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

(h) The amounts of the property, payroll, and sales of a partnership are attributable to the partners or members of the joint venture. A corporation that is a partner in a partnership must add its share of the property, payroll, and sales to its own apportionment factors, regardless of whether the partnerships are District of Columbia partnerships. The affiliated group should include a separate schedule to show the distribution to each partner.

(i) Apportionment factors are subject to the adjustments set out in §109.10, if necessary to clearly reflect income or to prevent the evasion of tax.

109.21-
109.29 [Reserved]

109.30 In computing the net income of the consolidated group, there shall be allowed a deduction for the consolidated net operating loss, in the same manner as allowed under IRC §§ 172 and 1502 and the federal income tax regulations thereunder and D.C. Official Code Section 47-1803.03(a)(14).

(a) Since an affiliated group filing a District consolidated return often does not include all the members included in the federal return, the net operating loss deduction is limited to the amount of deduction that would otherwise be allowed for federal income tax purposes had the federal return been filed including only the District of Columbia entities for the tax year involved. The federal consolidated return must be adjusted to reflect only District-source losses.

(b) Each member of a District of Columbia affiliated group shall have its own net operating loss deduction (before apportionment) for loss years prior to 2000 and D.C. apportioned net operating loss deduction (after apportionment) for loss years 2000 and thereafter where:

(1) such member filed a separate District of Columbia franchise tax return for years 2000 and thereafter, or
(2) such member was included in a different District of Columbia affiliated group for years 2001 and thereafter.

(c) The following is an example of the application of § 109.30(b):

Corporation A files a return on separate company basis for tax year 2000 and has a D.C.-apportioned net operating loss of $50,000 to be carried forward to subsequent years. For taxable year 2001, Corporation A joins with Corporation

B to file a consolidated return. Corporation A utilizes only $30,000 of its $50,000 D.C.-apportioned net operating loss from taxable year 2000 to the extent of its total taxable income of $30,000 for taxable year 2001.

Tax Year 2001	Corporation A	Corporation B	Consolidated Income
Total taxable income before apportioned NOL deduction	$30,000	$80,000	$110,000
Less apportioned NOL deduction	(30,000)		(30,000)
Total taxable income			$ 80,000
Carryover to 2002	($20,000)		

(d) If the District of Columbia affiliated group has a consolidated net operating loss carry forward from prior taxable years, the consolidated net operating loss of that District of Columbia affiliated group shall be carried forward and utilized by such District of Columbia affiliated group to the extent that such District of Columbia affiliated group has apportioned District of Columbia taxable income in future years.

(e) The following is an example of the application of § 109.30(d):

Tax Year 2001	Corporation M	Corporation N	Consolidated Income
Total taxable income before apportioned NOL deduction	$30,000	($80,000)	($ 50,000)

Tax Year 2002	Corporation M	Corporation N	Consolidated Income
Total taxable income before apportioned NOL deduction	$50,000	($20,000)	$ 30,000
Less apportioned NOL deduction			(30,000)
Total taxable income			$ -0-
Consolidated net operating loss carry forward to 2003 and beyond			($20,000)

(f) The Separate Return Limitation Year (SRLY) provisions of IRC §172 and IRC §1502, and the federal income tax regulations thereunder, shall apply in those cases where a member of a District of Columbia affiliated group which has a D.C.-apportioned net operating loss carryforward leaves the group and either files a separate District of Columbia franchise tax return or joins in the filing of a consolidated return with a different District of Columbia affiliated group. The

prorated amount assigned to each member who incurred the loss is determined by the following formula:

(A/B) x C = D
A/B = Ratio based on one corporation's loss to total corporation losses
C = Consolidated net operating loss
D = Prorated amount of consolidated net operating loss assigned to the member.

(g) The following is an example of the application of § 109.30(f):

In 2001 Corporations B and C were members of a District of Columbia affiliated group which had Corporation A as the common parent. On January 1, 2002 Corporation B and Corporation C became members of a different District of Columbia affiliated group the common parent of which was Corporation D.

The ABC consolidated group had a consolidated loss of $20,000 for tax year 2001.

Tax Year 2001	Corporation A	Corporation B	Corporation C	Consolidated Income .
Taxable Income	$100,000	$(80,000)	$(40,000)	$(20,000)

Calculation of Corporation B's share of Tax Year 2001 Consolidated Loss:

A = $(80,000) for Corporation B
B = $(120,000) for Corporation B and Corporation C
C = $(20,000) for consolidated loss

($80,000/$120,000) x $20,000 = $13,333 loss assigned to Corporation B

Calculation of Corporation C's share of Tax Year 2001 Consolidated Loss:

A = $(40,000) for Corporation B
B = $(120,000) for Corporation B and Corporation C
C = $(20,000) for consolidated loss

($40,000/$120,000) x $20,000 = $6,667 loss assigned to Corporation C.

For taxable year 2002, Corporation D, Corporation B and Corporation C have taxable income before NOL deduction of $80,000, $60,000, and $4,500, respectively. In this situation, Corporation B will utilize all of its $13,333 of D.C.-apportioned net operating loss carryforward from 2001, but Corporation C will utilize only $4,500 of its $6,667 D.C.-apportioned net operating loss carryforward from 2001 to the extent of its 2002 taxable income of $4,500.

The DBC consolidated group has a consolidated loss of $17,833 for the tax year 2002.

Tax Year 2002	Corporation D	Corporation B	Corporation C	Consolidated Income .
Taxable Income before apportioned NOL deduction	$80,000	$60,000	$4,500	$144,500
Less apportioned NOL deduction		(13,333)	(4,500)	(17,833)
Total taxable income				$126,667
Carryover to 2003			($2,167)	

(h) A surviving corporation in a merger is permitted to use District of Columbia net operating losses and District of Columbia apportioned net operating losses of a merged corporation, provided that the surviving corporation for federal tax purposes is permitted to use the federal net operating losses, if any, of the merged corporation. IRC §§ 381 and 382 apply with respect to the allowable loss.

109.31-
109.39 [Reserved.]

109.40 Special "Opt-Out" Rule for Qualified High Technology Company (QHTC): A corporation that qualifies under D.C. Official Code § 47-1817.01.(5)(A) as a QHTC may elect to join in the filing of a consolidated tax return with its affiliated group. By electing to join in the filing of a consolidated return, the corporation that would otherwise qualify as a QHTC shall be deemed to opt-out of QHTC status on a permanent basis. Such corporation and its affiliated group shall, by joining in the filing of a consolidated return, be permanently estopped from qualifying for tax benefits under D.C. Official Code §47-1817.

109.41-
109.99 [Reserved.]

All persons interested in commenting on the subject matter in this proposed rulemaking may file comments in writing, not later than thirty (30) days after the publication of this notice in the D.C. Register, with the Office of Tax and Revenue, ? Office of the General Counsel, 941 North Capitol Street, N.E., Suite 810, Washington, DC 20002.